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# **An Assessment of Budgeting and Budgetary Controls among SMEs: Evidence from a Developing Economy**

## **Abstract**

**Purpose:** The capacity to plan, manage, and control small and medium enterprises (SMEs) is critical to realising their organisational goals. This paper assesses the effectiveness and perception of budgeting and budgetary control systems among SMEs.

**Design/Methodology:** Relying on the goal-setting theory (GST) and a methodology that accommodates questionnaires, data was collected from 170 manufacturing SMEs located in Cape Town, South Africa.

**Findings:** Research results affirm that the deployment of budgeting benefits from a positive perception of the value of budgeting and budgetary controls by key SME stakeholders. The study also finds that the perception of budgeting mirrors the level of education of SME operators, as educated respondents understand the value of implementing robust budgeting systems. Despite its focus on manufacturing SMEs, this study suggests that the manufacturing budget is the least utilised budgeting system among these organisations.

**Practical implications:** The study reinforces the communication power of budgeting and budgetary controls as SMEs and economic agents are not only aware of corporate objectives but are equally incentivised to support the attainment of these objectives.

**Originality/Value:** Despite the extensive application of GST among scholars, its use in budgeting and budgetary control literature, particularly among SMEs in developing contexts, is limited. In line with GST, this study indicates that when agents establish and implement a plan, they are motivated to pursue and realise the set expectations while consistently evaluating themselves for improvement opportunities.

**Keywords:** SMEs, budget, budgetary control, goal-setting theory, manufacturing sector

**Article Classification:** Research paper

## Introduction

Budgeting serves different roles in contemporary organisations (Davidson, 2009). Drury (2018) enumerates these roles to include *planning* annual operations, *coordinating* the organisation's activities, *communicating* plans, *motivating* managers, *controlling* activities, and *evaluating* managers' performance. Given its broad scope, budgeting is a critical driver of organisational performance. Therefore, it is unsurprising that the impact of budgeting and budgetary controls on firm performance has attracted considerable interest among scholars (Lidia, 2015; Pimpong and Laryea, 2016; Laitinen et al., 2016). In the absence of budgeting, Laitinen *et al.* (2016) explain that organisations suffer from resource underutilisation.

While budgeting ensures prudent planning of an organisation's future performance (Gooneratne and Hoque, 2016), budgetary control offers frameworks that enable management to compare actual results with targets and implement corrective measures when deviations occur (Cohen and Karatzimas, 2011; Mohamed *et al.*, 2016). This understanding of budgetary control has motivated greater curiosity among scholars (see, for example, Frow, Marginson and Ogden, 2010; Dunk, 2011; Kerosi, 2018). However, the literature in this domain suffers from two significant limitations. First, the budgetary control scholarship has typically studied large companies to the detriment of smaller organisations. Second, most of the research in this space investigates companies in the western world (see, for example, Hansen and van der Stede, 2004; Laitinen *et al.*, 2016), ignoring the contextual issues that may stimulate contrasting outcomes from SMEs in developing economies (Lopez and Hiebl, 2015; Zor *et al.*, 2019).

Regarding Africa, very few studies (e.g., Onduso, 2013; Maritim, 2013; Kerosi, 2018) explore the concept of budgetary control. Notably, South African manufacturing SMEs have attracted minimal interest in this research domain. While South Africa is Africa's largest economy, some contextual peculiarities emphasise its adoption in this study. First, its business environment is mostly informal (Etim and Daramola, 2020), with implications for the perception of budgeting and budgetary control among entrepreneurs. Second, the country has multiple cultures, and its economic agents believe in deep-rooted local traditions that conflict with Western ideologies, e.g., the Ubuntu notion is inconsistent with the West's shareholder wealth maximisation idea. Also, given the sizeable presence of state-owned enterprises, the country's government is a major player in its business environment. Consequently, the state influences market dynamics, which may impact budget operationalisation among firms.

As the leading economy in Africa, its manufacturing SME sector is pivotal to the economy and the African continent, especially given the need to support the global value chain (Urban and Naidoo, 2012). South African SMEs contribute significantly to the country's gross domestic product (GDP) and ranks among the highest employers of labour (Bayramov *et al.*, 2017). SME South Africa (2018) also reports that 71% of SMEs generate a maximum of R200 000 per annum, while 20% generates between R200 000 and R1 000 000 annually. Besides, the advent of COVID-19 has made it inevitable for the country to strengthen its entrepreneurial capacity by supporting SMEs to become principal players in commodity production. Against this backdrop, SMEs should leverage the benefits of budgeting and budgetary control to maximise their performance. Therefore, despite the challenges in the South African business environment, it is crucial to understand the role of budgeting and budgetary control on SMEs' operations in the country's manufacturing sector.

To address the preceding, we articulate two central objectives for this study. The first objective is *to explore the perceptions of budgeting and controls on business performance among manufacturing SMEs*. Given the concerns regarding culture and tradition, we opine that it is critical to investigate SMEs entrepreneurs' perception of budgeting. The second objective is *to evaluate factors that influence the establishment of budgetary controls among manufacturing SMEs*. While the latter objective has gained traction, we anticipate that the South African business environment provides an alternative context to generate fresher insights that extend the scholarship in this field.

To address the above objectives, we embrace the goal-setting theory (see Locke and Latham, 1984, 2006, 2013; Pepper and Gore, 2015) to enable us to capture the connections between perceptions of budgeting, drivers of budgeting, budgetary control, budgetary goals and performance. This study adopts the survey method that permits data collection using questionnaires (Balnaves and Caputi, 2001; Maelah and Yadzid, 2018). Our analysis of the data allows us to contribute to the literature by presenting budgetary control as a critical control system for enhancing SMEs' wealth-generating potential among South African manufacturing SMEs. This article also demonstrates how the preceding finding benefits from a positive perception of budgeting and budgetary controls by SME entrepreneurs and managers. This research further finds that the perception of budgeting mirrors the level of education of SME operators, as educated respondents understand the value of implementing robust budgeting systems in their firms. This finding suggests that the perception of budgeting is low in environments with lower levels of education. Findings in this paper enrich the extensive

literature of budgeting and budgetary control but, more specifically, shed interesting insights into SMEs' overlooked areas, particularly among developing economies.

The rest of this paper is structured as follows: First, this study presents the underlying theory and reviews the literature examining the linkage between organisational objectives, budgetary control and business performance. This is followed by a discussion of the study's methodology. The authors then present and discuss the data emphasising how budgetary control and perceptions of budgeting impacts SMEs in a developing economy. Lastly, the authors highlight the implications of this study's findings, articulate its limitations, propose recommendations, and identify future research areas.

## **Theory and Literature Review**

### ***Goal-Setting Theory (GST)***

A central element in modern budgeting is the nexus between corporate goals, firm productivity, and employee commitment (Pepper and Gore, 2015). Scholars have adopted a range of theories to explore the relationship, but there is a considerable engagement with GST in this research field (see Locke and Latham, 2006; Kleingeld *et al.*, 2011; Curseu *et al.*, 2014; Pepper and Gore, 2015). GST emphasises the robust connection between goals, commitment, and performance (Lunenburg, 2011; Pepper and Gore, 2015) and the development of strategies to motivate and guide individuals towards accomplishing goals. While Marsden and Richardson (1994) stress the merit of setting achievable, acceptable, clear, and measurable work goals, GST contends that specific and challenging goals with appropriate feedback strategies contribute to higher task performance (Latham, 2004; Locke and Latham, 2013). Moreover, GST extends the scope of the goal, performance, and commitment connection, implying that assigning specific goals does not solely result in improved performance but increases motivation and performance when individuals accept these goals and the associated difficulty (Ambrose and Kulik, 1999; Atkinson and Shaw, 2006; Smith, 2006).

Goal setting is beneficial when there is a feedback system highlighting the progress towards objectives (Consolvo *et al.*, 2009). The control (feedback) mechanism characteristic of GST ties with budgetary control systems, even more among SMEs. For instance, SMEs' budgetary control systems offer a feedback mechanism that indicates progress towards predetermined budgetary goals and employee motivation to set goals. Taking GST into perspective, SMEs'

willingness to accept the difficulty associated with measuring and monitoring budgetary control systems to achieve set objectives motivates the identification of deviations and the subsequent implementation of proactive corrective measures. This process triggers an effective and efficient cost-saving budgeting mechanism that supports SMEs' performance.

Given its utility, several studies adopt GST. Brandstätter *et al.* (2003) employed the theory to investigate students' retraining needs in continuing education. The research suggests that combining goal (and implementation) intentions helped initiate vocational retraining that supports corporate objectives. Consolvo *et al.* (2009) utilise GST to examine how persuasive technologies encourage physical activity and to understand the reactions of individuals to goal sources (who sets the goals) and goal timeframes (goal achievement period). Furthermore, Latham and Pinder (2005) explore the effects of goal setting in the workplace, investigating how various goals affect employees' performance and motivation while discharging their responsibilities. Chienwittayakun and Mankin (2015) embark on similar studies, using GST to link goals and objectives with employee engagement and performance. GST equally found relevance in broader organisational literature such as behavioural ethics (Welsh and Ordóñez, 2014), leadership and vision communication (Berson *et al.*, 2015), gender and ethnic minority (Schipper *et al.*, 2015), and educational video games (Nebel *et al.*, 2017), among others.

The budgeting literature has also engaged with GST. Onduso (2013) applied the theory to investigate budgetary effects on the performance of manufacturing firms. The research indicates that budget and managerial performance influences financial performance. Likewise, Faith (2013), employing GST in a study involving manufacturing parastatals, concludes that budget planning and control promote sales growth and profit. In another evidence from state-owned enterprises, Simpson (2013) employs GST to demonstrate how a lack of employee commitment hampers budgetary objectives, even when goals have been established and communicated appropriately. This outcome is consistent with Smith (2006), given the broader factors that may influence employee commitment. Indeed, Khin *et al.* (2014) suggest that the perception of fairness mediates the relation between budget participation levels and goal commitment, while goal commitment mediates the connection between the perception of fairness and performance. This view unearths the link between goal setting and fairness because if goals are deemed unfair, it could impact employee commitment. Khin *et al.* (2014) conclusion compares with earlier research by Chong and Chong (2002), which indicates that budget participation, especially in budget goal commitment and shared information, positively impacts job performance. These evidence suggest that establishing a robust mechanism for setting budgets creates a culture of

efficiency and effectiveness that stimulates the attainment of budgetary goals (Onduso, 2013, Zwikael *et al.*, 2018). This also underscores employees' organisational commitment and how it contributes to favourable business performance.

While the preceding studies uncover the relevance of GST in this research, we note that the GST literature is yet to fully explore areas that could enrich the understanding of the theory. These areas include how goals may lead to 'creative' responses by agents, the potential for goal setting to provoke unethical behaviour, incentivise bad behaviour, and debate that goal setting focuses on individuals rather than organisations. Given its broad appeal, this paper sets out to contribute to the GST debate, drawing insights from the less studied SME sector in a developing economy. Precisely, on the one hand, we embrace GST to examine how perceptions of budgeting and control are crucial to business performance. On the other hand, goal setting benefits from budgetary control systems deployed to provide feedback on progress towards desired objectives, as this improves perception. Numerous factors, such as assumed fairness and origins of goals (i.e., who sets them?), influence perceptions. This article proceeds with a literature review to stress the lacuna in this research area.

### ***Budgeting in SMEs***

Budgets aid the coordination of the various parts of an organisation, i.e., controls and measures employee performance, motivates personnel and increases communication (Fisher *et al.*, 2002; Hansen and van der Stede, 2004; Parker and Kyj, 2006; Heupel and Schmitz, 2015). Budgets are management control systems (MCS) that influence managers' behaviour and decisions in translating business objectives into a plan of action, communicate goals, and provide benchmarks to assess performance (King *et al.*, 2010; O'Grady and Akroyd, 2016). Joshi *et al.* (2003) and Heupel and Schmitz (2015) further clarify that budgets are a subset of performance measurement employed by organisations to quantify plans for a defined period.

Given the above, accomplishing organisational objectives is critical to firms, considering that evaluation of firm performance builds on the variance between the budget and actual results (Joshi *et al.*, 2003; Cohen and Karatzimas, 2011). The preceding literature also advocates that evaluation links directly to rewards systems, indicating that the use of budgets for evaluation coerces organisational agents to improve performance. In relation, Cohen and Karatzimas (2011) emphasise that clear targets improve performance compared to uncertain goals,

resulting in dissatisfaction and frustration among employees. Also, while Otley (1978) affirms that organisations that adopt budgeting as a medium for establishing corporate goals tend to earn desired outcomes, Mohamed and Ali (2013) concur that budgeting systems that set out concrete objectives have a significant positive relationship with corporate performance.

Whereas the literature (Hillidge, 1990; Knight and Knight, 1993) has focused on investigating the impact of budgeting and business performance, studies (Wijewardena *et al.*, 2004; Frow *et al.*, 2010; Daumoser *et al.*, 2018) exploring the role of budgeting among SMEs are not only limited but have also reported inconsistent findings. Though Augustine *et al.* (2012) recognise that budgetary control is a vital mechanism among SMEs, evidence suggests that SMEs do not have formal budgetary systems due to a perception that dilutes budgeting significance. This perception stems from the undesirable effects of budgeting (Drury, 2018), prompted by a dearth of appropriate expertise to execute budgets among SMEs and a lack of top management support (Maduekwe and Kamala, 2016). Mutanda (2014) adds that SMEs lack the underlying motivation to prepare budgets, as they do not understand its impact on their business.

Despite these concerns, Dunk (2011) recommends that SMEs must implement budgetary controls as a planning tool to allow creativity and innovation to flourish in their organisations. Heupel and Schmitz (2015) also advocate that budgets and budgetary controls should be flexible and adaptable to developments in the business environment to enhance the potential of achieving desired goals. Badem (2016) and Daumoser *et al.* (2018) contend that the propositions in Dunk (2011) and Heupel and Schmitz (2015) must accommodate the establishment of formal systems that allows for continuous monitoring and control of the process and the evaluation of actual outputs against plans. This is critical, as findings in Kamau *et al.* (2017) reveal that formal control systems improve budget performance.

Given the challenges in its institutional and business environments, the above views are pertinent in South Africa. In a 2018 report by SMEs South Africa that exposed some fundamental findings on the country's SMEs landscape, the report notes that South African SMEs are repeatedly denied funding due to insufficient cash flow and operational history. This infers that engagement with budgeting and budgetary controls may curb these challenges. But the literature that supports the preceding notion is scarce. Maduekwe and Kamala (2016) note that limited studies have been conducted in South African on budgeting and budgetary control for SMEs. Pimpong and Laryea (2016) remark that many studies examine budgeting and



budgetary control issues drawing insights from diverse contexts but observe that SMEs in South Africa had been largely overlooked.

Qi (2010), for instance, researches the impact of budgeting on SMEs' performance in China, while Wijewardena and Zoysa (2001) examined the effect of planning and budgetary control on Australian SMEs' performance. Jermias and Yigit (2013) research budgetary participation and its impact on information asymmetry, goal commitment, and role ambiguity on Turkey's job satisfaction and performance, reporting that goal commitment and complexity of roles influences performance. Macinati and Rizzo (2014) investigate the link between goal commitment, budgeting information and firm performance in Italy. Zor *et al.* (2019) study CEO characteristics and budgeting practices among SMEs in Turkey and found that education and experiences are positively associated with adoption and the extent of budget use.

On the African continent, Onduso (2013) focuses on the effects of budgeting and financial performance in Kenya, while Maritim (2013) relies on the same context (Kenya) to study the influence of budgeting on SMEs' financial performance of SMEs. Adongo and Jagongo (2013) provide empirical evidence of budgetary control in Kenya's state corporations' performance. They find a significant positive relationship between budgetary control and state corporations' financial performance, explaining that the influence of budgetary controls on corporate objectives, funds allocation, and firms' investment choices accounts for this result. This finding is relevant even to SMEs as they (Adongo and Jagongo, 2013) further observe that budgeting helps organisations predict their financial milestones. However, to attain Adongo and Jagongo (2013) expectations, Zor *et al.* (2019) argue that education and experience are pivotal in adopting and engaging with budgeting and budgetary controls. Such attributes, i.e., education and experience, produce a perception that underpins and motivates the use of budgeting. The budget perception remains a critical component of the successful implementation of budgeting, but a negative perception could harm the intended outcomes of budgeting.

### ***Perceptions of budgeting***

The usefulness of budgeting derives from entrepreneurs and managers' perception. Aliabadi *et al.* (2019) contend that organisations desirous of transforming budgeting should reflect on their key stakeholders' perceptions of the budgeting process. They note that such reflection helps identify and solve any loose coupling that may emerge from internal, external and behavioural

circumstances. Given the need to understand the perception of budgeting among preparers and users, it is unsurprising that there has been substantial interest in the perception of budgeting and its implications for companies. Kim and Mauborgne (1993) note that when senior managers perceive that organisational procedures are fair, such executives exhibit higher organisational commitment and compliance with corporate policies. Thus, such managers are more likely to participate and cooperate in attaining budgetary goals. Pasewark and Welker (1990) and Libby (1999) also contend that the extent of participation is critical to budgeting perception. They note that where there is a perception that the budgeting process is pseudo-participative, subordinates (users/implementers of the budget) are unlikely to commit to budgeting objectives. This suggests that stakeholders' participation in establishing budgets enhances their perception of budgeting.

The literature unearths factors that impact budgeting perception. Neely *et al.* (2001) identify twelve commonly referenced budgeting deficiencies (see also Hansen *et al.*, 2003). These shortcomings amplify the negative perception of budgeting. Besides, the budgeting process produces behavioural issues in the way people work. For instance, Jansen (2001) reports that budgeting provides managers with opportunities to lie, cheat, and promote unethical internal competition that typically pitches colleagues against themselves. Neely *et al.* (2003) and Libby and Lindsay (2010) also emphasised the time implications of budgeting. Neely *et al.* (2003) observe that the budgeting process utilises more than 20% of managers time, while Libby and Lindsay (2010) criticised the budgeting procedure for consuming too much time.

Despite these concerns, the often-cited positive implications of budgeting (see Lindsay and Libby, 2007; Shastri and Stout, 2008) demand that firms continue to explore how budgeting contributes to corporate objectives. The perception of budgeting is central to the forgoing expectation. Therefore, establishing robust budgetary systems reinforce the relevance of budgeting among firms.

As stakeholders acknowledge the relevance of budgets, their perception of the process intensifies. Considering the gains of budgeting, such budgeting perception of budgeting and budgetary controls maximises their business performance.

### ***The nexus between budgetary control and business performance***

The link between corporate goals and firm performance benefit from elements that include budgeting. Heupel and Schmitz (2015) theorise that SMEs can reap budgetary control gains if managers and employees adhere to the organisation's budgetary requirements. Budgetary goals influence managers and employees' behaviour (Frow *et al.*, 2010; Heupel and Schmitz, 2015). An effective budgetary control system allows managers and employees to become conscious of their future financial objectives (Hansen and van der Stede, 2004; Heupel and Schmitz, 2015; Gooneratne and Hoque, 2016). Dunk (2011) and Nazarova *et al.* (2016) advocate that SMEs can profit from formal business plans because it provides the groundwork for setting objectives, generating and evaluating strategies, monitoring and committing to their implementation while maintaining effective communication with its diverse stakeholders. On this evidence, budgeting amplifies efficiency through planning and coordination; supports the learning and control when comparing actual results with plans; and the capacity to weave all the disparate threads of an organisation into a comprehensive plan to serve various purposes (Nazarova *et al.*, 2016; Daumoser *et al.*, 2018).

However, the gains associated with adopting formal budgeting practice may not be "one size fits all" (particularly among SMEs), which are usually dependent on business-specific contextual factors (King *et al.*, 2010; Heupel and Schmitz, 2015; O'Grady and Akroyd, 2016). There are also concerns associated with a structured and sophisticated approach to planning and control in SMEs (Sexton and Van Auken, 1985; Lorain *et al.*, 2015). Dokulil *et al.* (2017) posit that a lack of adaptability to the continuously evolving business environment undermines budgeting value. Similarly, Frow *et al.* (2010) note that the literature concedes that the undesirable attributes of budgeting, such as the constraint to learning and innovation, impede organisational performance. Besides, a high degree of emphasis on budget attainment may create side effects that could lead to a dysfunctional firm (Bartlett and Ghosal, 1993; Hope and Fraser, 2003). Concerns stemming from a dysfunctional firm accelerates job-related tension, group-based anti-management behaviour, short-termism and data manipulation (Dokulil *et al.*, 2017). These challenges, nonetheless, the literature extensively explores the connection between budgetary control and financial performance. As this study focuses on SMEs, we examine the link between budgetary control and SMEs' financial performance in the next section.

### ***Budgetary control and financial performance among SMEs***

Whereas the preceding section examines the relationship between budgetary control and business performance, it is equally useful to understand how budgetary control impacts a central component of organisational performance, i.e., financial performance. The existing literature explores the link between budgetary control and financial performance among SMEs. Nwanyanwu and Ogbonnaya (2018) report a significant relationship between SMEs' budgetary control and financial performance, contending that budgetary control propels SMEs' growth and sustainability if efficiently deployed. Wijewardena *et al.* (2004) and Nazarova *et al.* (2016) add that effective control is necessary to achieve desired results from set financial plans. Thus, SMEs must measure actual financial performance against their objectives periodically and identify deviations to implement appropriate corrective measures. Furthermore, Wijewardena *et al.* (2004) emphasise that a robust planning and control system is essential to improve SMEs' financial performance. This finding implies that the greater the extent of sophistication in planning and control, the better its financial performance.

A blend of factors impairs the impact of budgetary controls on SMEs' financial performance. Bianchi (2002) and Nwanyanwu and Ogbonnaya (2018) insist that smaller firms lack the needed managerial skills and financial resources. This prohibits effective engagement with formal control systems that support robust financial outcomes. The absence of these elements frustrates the fundamental pillars of GST as feedback and feedforward systems are either not established or grossly ineffective. Furthermore, a lack of education and training contributes to SMEs' sub-optimisation, stifling anticipated financial performance (O'Neil and Duker, 1986). Despite these failings, King *et al.* (2010), Heupel and Schmitz (2015), and Dokulil *et al.* (2017) maintain that the extent of budget deployment among SMEs is positively associated with structure (decentralisation) and strategy (cost leadership), but negatively associated with perceived environment uncertainty (dynamism). Even so, much of the literature in this domain (e.g., Dunk, 2011) contends that budgets are likely to enhance the financial performance of a firm, particularly when used primarily as a planning mechanism. This is consistent with the results in Wijawardena and Zoysa (2001), Qi (2010), Faith (2013), and Pimpong and Laryea (2016), which demonstrate that budgetary control improves the financial performance of SMEs significantly.

## Research Methodology

### *Data Sampling*

This study, conducted in Cape Town, South Africa, focused on SMEs in the manufacturing sector. The research focuses on manufacturing SMEs that have been in operation for more than a year, with less than 200 employees. Researchers identified the sample from the City of Cape Town Municipality industrial database, which contains information relating to the Western Cape Province's manufacturing companies. The total population of SMEs in these industrial areas is 2477. To reach an appropriate profile of respondents, the authors focused on entrepreneurs, operational and finance managers, given their knowledge relative to our research objectives. Besides, related studies (Teddlie and Yu, 2007) rely on these participants, given their engagement with their organisations' budgeting process. The authors employ a random sampling technique to recruit respondents. We used the Yamane formula to determine an appropriate number of respondents for this study. The Yamane formula is computed as:

$$n = N/(1+Ne^2)$$

where  $n$  is the corrected sample size,  $N$  represents the population size, and  $e$  (the margin of error), typically denoted by 0.05. While the Yamane formula is appropriate for determining the sample size when working with a finite population and the population size is known (Singh & Masuku, 2014), the above formula produced a corrected sample size of approximately 344, i.e.,  $n = 344$ . The calculated  $n$  value helped in establishing a target for data collection.

### *Data Collection: Closed-Ended Questionnaire*

A questionnaire was used to collect data for this research (see Appendix 1). The questionnaire contained closed-ended questions to ensure objectivity (Rowley, 2014). The items in the questionnaire were informed by the research objectives (Dillman, 2011). The questionnaire, complemented by the knowledge gained from the literature review, emphasised core elements of budgetary control systems practices, budgetary control impact and budgetary perceptions among preparers and users (i.e., owners, managers) of budgetary information. Researchers adapted King *et al.* (2010) instrument on the frequency of operational budget use, where they employ a five-point Likert scale that includes yearly, half-yearly, quarterly, monthly and weekly. Researchers also followed Dillman (2011) and Albu and Albu (2012) suggestions of pretesting the questionnaire using management accounting academics and selected SMEs. This pilot helped in checking the correctness and understandability of the questions in the questionnaire.

Before actual piloting, we engaged three management accounting academics to offer feedback regarding the questionnaire design. In doing this, we relied on Malmqvist et al.'s (2019) suggestion to hire experts to design survey instruments before piloting. After that, we identified five respondents from manufacturing SMEs for the actual pilot to assess whether we needed to make further improvements (e.g., ease of comprehension, use of language, etc.) in the questionnaire. Overall, the authors were pleased with the completion of the questionnaires as there were minimal errors in the returned questionnaires. Similarly, feedback from the academics that reviewed the design was generally positive.

Following the pilot's conclusion, the authors enlisted accounting undergraduates to help distribute the questionnaires. These students are in the final year of an undergraduate programme and have just completed a research methodology course. While authors secured ethical approval from a university before engaging the students, we hired these students to allow them to gain valuable experience in conducting surveys. Also, considering the spread of potential participants, the students helped reach more participants and ensured timely data collection. The questionnaires were distributed with the consent letters. The consent letters included a clause that promised the confidentiality of participants. Participants were also informed that they could withdraw from the data collection at any time.

Necessary steps were also taken to ensure that no participant suffered any harm from participating in the study. However, due to access concerns and the general apathy to research activities by SMEs in developing economies (Nel *et al.*, 2017), researchers could not achieve the targeted sample size because of SME managers' unavailability. In some cases, despite promises by potential participants to complete the questionnaires, several visits and calls to possible respondents did not yield any positive outcome. This challenge impeded our initial data projection (determined using the Yamane formula) as 215 managers did not participate in the study. In total, we collected 185 questionnaires. Following the checks on the returned questionnaires, we discarded 15 of them. The discarded questionnaires were deemed unusable for our analysis as the managers did not complete the whole questionnaire.

Consequently, the remaining 170 questionnaires were fully completed and found useful for this study. Therefore, this study relied on data sourced from 170 SMEs operating in the manufacturing sector in Cape Town, South Africa. Laitinen *et al.* (2016) report a response rate of 27% from 500 selected sample of manufacturing firms. King *et al.* (2010) received only 14.6% from 1000 selection sample and confirmed its comparability to the response rate in small

business research (Dennis, 2003). Therefore, the 49% response rate from a targeted sample size of 344 in this study falls within a reasonable margin of response rate in small businesses.

The questionnaire was divided into four sections. Section A entailed 'yes or no' questions, including categorical questions based on budgetary control system practices. Section B focused on the impact of implementing a budgetary control system, comprising five (5) Likert scale questionnaire items ranging from 1= never, 2= rarely, 3= sometimes, 4= frequently to 5= very frequently. Section C, which focused on budgeting perception, comprised Likert scale questionnaire items stretching from 1= strongly disagree, 2= disagree, 3= undecided, 4= agree to 5= strongly agree. Lastly, section D contained information relating to the demographics of the study participants.

### ***Data Analysis***

Following the collection of data, we analysed the responses from the questionnaires. The analysis commenced by preparing grids to collate the data in the questionnaires. The grids were designed to correspond with the Likert scale used in developing the questionnaires. As this study adopts the Likert scale, there was no need to code the responses. Data were recorded on the grids, followed by calculating the proportion of participants response for each category of questions. Throughout this procedure, authors relied on the Statistical Package for Social Sciences (SPSS) software to eliminate possible human errors during data analysis. Authors used the software to generate relevant statistical information such as percentages, means, modes, standard deviations, frequency counts, among others (see Tables 2-12).

Before the data analysis, the reliability of the scales used in this study was assessed to determine internal consistency and measure the scale's reliability (see Tsang, Royse and Terkawi, 2017). To achieve this, the authors utilised Cronbach's Alpha, which stipulates that a reliability coefficient of 0.7 or higher is considered "acceptable" and reliable in social science research (Hardy and Bryman, 2009, Sekaran and Bougie, 2016). Table 1 shows a Cronbach's Alpha value of  $\alpha = 0.85$  for the impact of budgetary control, signifying that each of the budgetary Likert scale items is reliable. Furthermore, the alpha ( $\alpha$ ) value for budgetary perception is  $\alpha = 0.88$ , denoting that it is equally reliable, given its relatively high internal consistency.

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**Table 1 about here**

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## **Data Presentation and Analysis**

From Table 2, the findings show that 48.2% of participants outsource the budgetary control system, while 51.8% undertake the responsibility inhouse. The majority (87.1%) of participants acknowledge that budgetary control systems play an essential role in planning the business's future. 84.7% of participants employ budgets to control business operations, with 88.2% utilise budgets to compare actual performance against projections. Most (80.6%) participants follow set procedures to evaluate the variation between planned and actual budget performance, even as 77.6% of participants are satisfied with the budgetary process adopted in their business. These results suggest that budgetary control systems are essential for SMEs' present and future operations. These responses infer that manufacturing SMEs comply with regulations governing budgeting and budgetary procedures. These replies further imply that participants prefer internal budgetary control systems compared to outsourcing.

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### **Table 2 about here**

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A significant number of SMEs (87.7%) admit that budgetary control systems play an essential role in planning their organisations' future direction. This is consistent with Nazarova *et al.*'s (2016) conclusion, stressing the strategic necessity for budgeting. Cohen and Karatzimas (2011) affirm that budgetary control systems help assess the variance between budgeted and actual results, critical to corporate survival. Budgetary control systems enable businesses to set specific business goals. This activity provides substance to management policy and strategy, supporting corporate goals (Lorain *et al.*, 2015; Nazarova *et al.*, 2016).

## **Frequency of Budgeting**

The perception of budgeting and controls on corporate informs how frequently users employ budgeting to review and track their performance. Participants indicate varying budgetary control review timeframes, with 6.5% reviewing budgets weekly, 35.3% reviewing every month, 21.2% reviewing quarterly, 19.4% semi-annually, while 17.6% review their budgets annually (see Table 3). In terms of budget preparation, 6.5% prepare the report every week, 30.0% every month, 28.8% every quarter, 18.8% every half year, and 15.9% yearly. The participants also indicated that management undertakes a financial performance review at



predetermined times as follows: 4.1% weekly, 31.8% monthly, 29.4% quarterly, 14.7% half-yearly, and 20.0% yearly.

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### **Table 3 about here**

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The results suggest that SMEs in the manufacturing sector update, review, and prepare budgets at different times during the year. SMEs do not engage in "one-size fits all" as there is no evidence of a consistent time frame for preparing and reviewing budgets. This implies that firm attributes such as size, operational scale, number of employees, among others, influence their budgetary practices. King *et al.* (2010) and Lorain *et al.* (2015) concur that the frequency of budget reviews depends on business-specific goals and contextual factors. However, evidence from Lorain *et al.* (2015) revealed that many businesses review their budgets monthly. This coincides with our findings as most SMEs in this study (35.3%) engage in a monthly review of their budgets. This is helpful for SMEs, given that Badem (2016) recommends monthly budget reviews to identify budget deviations and rectify such deviations as they become necessary. A higher frequency of budget reviews enhances organisational flexibility and its capacity to respond to business developments, especially in a volatile business environment. However, the increased frequency of budget review could trigger adverse effects on the firm's financials, especially among SMEs that are limited financially (Nwanyanwu and Ogbonnaya, 2018). While it is imperative to note that an effective budgetary control system minimises wastages and costs, SMEs' responsibility is to establish a point of equilibrium where benefits achieved from budgeting compensate for the additional cost in increased budget review frequency. Still, the low level of financial literacy among South Africa SMEs (Fatoki, 2014) may frustrate the desired cost-benefit payoff.

### **SME's Budget System**

Table 4 shows that 22.9% of the participants use the 'production budget' system, 9.4% implement a manufacturing overhead budget system, 44.7% utilises the cash budget system, 8.2% engage the direct labour budget system, and 14.7% employ raw material purchasing budgets. This finding shows that manufacturing SMEs use different budgeting systems. Yet, there is a significant variation in preference among SMEs regarding the form of budget used. The most prevalent budget used is the cash budget system. This is unsurprising given the

importance of cash management to SMEs' survival in South Africa (Aren and Sibindi, 2014; Enow and Kamala, 2016). It is, however, interesting to note that while the participants were selected from SMEs in the manufacturing sector, the manufacturing budget is the least utilised budgeting system (9.4%). Given SMEs' well documented financial constraints, the need to prioritise may have accounted for this development. Other budgeting systems such as production budget, direct labour budget, and raw material purchasing (see Table 4) are manufacturing components. Therefore, respondents may have paid more attention to these areas at the expense of the manufacturing overhead budget.

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#### **Table 4 about here**

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#### **Budget Deviation Rectification**

From Table 5, the majority (44.7%) of participants seek to find the cause of budget deviation, 21.8% engage in re-planning when variations arise, while 18.8% implement new controls. The remaining participants (14.7%) outsource to fix budget deviations. By adopting strategies to identify the reasons for deviation from the budget, our data imply that most SMEs in the manufacturing sector acknowledge and take responsibility for budget deviations. Such intervention improves SME operators' knowledge regarding the usefulness of 'control' in management decision-making, minimising the future occurrence of such deviations. Paying attention to budget deviation and its triggers suggests that SME operators understand the inherent benefits of robust budgeting systems.

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#### **Table 5 about here**

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#### **Budgetary Control Impact**

This study also assessed the impact of implementing budgetary control systems, the responses of which are presented in Table 6. Most participants (40.0% and 52.4%) indicated that frequent budgetary controls help bring new ideas and attain their corporate targets, respectively. 45.9.0% of participants imply that frequent budgetary control system implementation assists in

identifying problems. Similarly, 51.27% of the participants hint that implementing frequent budget control improves decision making and communication between top and lower-level managers. Table 6 reveals that participants use budgetary control for various budgeting activities such as planning - never (1.2%), rarely (2.9%), sometimes (20.0%), frequently (42.9%), and very frequently (32.9%). Participants also indicate that establishing a budgetary control system (sometimes - 25.9%; frequently - 38.8%) limits potential financial crisis among SMEs. These responses, consistent with the literature, denote that the implementation of budgetary control systems is essential for coordination and strategic planning among SMEs. The literature (Fisher *et al.*, 2002; Parker and Kyj, 2006; Daumoser *et al.*, 2018) concedes that budgetary controls support organisational coordination, facilitate control and measurement of employee performance, identifies and solves business problems, motivates personnel and increases organisation-wide communication. Dunk (2011) accepts that budgets are likely to enhance the financial performance of a business. These views connect with GST (Locke and Latham, 1984) that assigning specific goals trigger performance improvements.

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#### **Table 6 about here**

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A total of 30.0% (never - 9.4% or rarely - 20.6%) suggests that they do not rely on budgetary control systems to decide wage increases. This is a concern given that wages account for a considerable fraction of business overheads. The findings also expose the impact of budgetary control system implementation on price increase of raw materials (never - 4.7%; rarely - 9.5%; sometimes - 30.8%; frequently - 40.2%; very frequently - 14.8%) and on unplanned operational expenses (never - 5.9%; rarely - 12.4%; sometimes - 25.9%; frequently - 40.6%; very frequently - 15.3%). In sum, these findings show that SMEs are conscious of other important factors when making decisions on raw material prices, wage increases, and unplanned operational expenses. In contrast, Memon (2014) emphasise that fluctuations in raw materials prices impact business budgets. Lack of budgeting knowledge influences budgetary control system implementation, as reflected in the following findings - never (10.6%), rarely (22.9%), sometimes (25.9%), frequently (27.6%), very frequently (12.9%). The findings compare with Table 5, where 14.7% of the participants are unaffected (never) by lack of budgeting knowledge as these participants outsource their budgeting function. This signifies that not all SMEs in the manufacturing sector execute budgeting internally. Still, a minimal number of

SMEs outsource their budgeting responsibilities in their entirety. This view connects with Sen and Haq (2010), which contend that manufacturing SMEs are more dominant in outsourcing non-core activities of their business than bigger firms.

Table 7 shows that all the elements 'mean' are above  $\bar{x}$  3.00, and the modes are  $M_o = 4$  (Frequently) for all the factors except for wage increase with a mode of 3 (Sometimes). These scores are high given that 5 (very frequently) was the maximum. The standard deviations are smaller, implying that the participants' responses are clustered more closely to the mean and the mode. From Table 7, the most critical impact of the budgetary control system is on planning with a mean of  $\bar{x} = 4.04$  and a standard deviation of  $\sigma = 0.870$ . Conversely, wage increases are not significantly determined by the budgetary control system outcomes, suggesting that other factors influence manufacturing SMEs' wage decisions. Additionally, this can be attributed to the increased wages that are predictably implemented annually.

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#### **Table 7 about here**

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### **Budgetary Perceptions**

We also examine the perceptions of SMEs regarding budgeting. Table 8 reveals that most participants agree (42.4%) or strongly agree (25.3%) that budgetary controls are central to SMEs' operations. 75.3% of the participants acknowledge that budgetary controls are implemented by skilled and experienced managers, inferring that lower-level employees are seldom involved in implementing budgetary controls. This underscores the importance attached to budgetary controls by manufacturing SMEs in South Africa. Moreover, this ties with Zor *et al.* (2019), asserting that education and experience inform the adoption and extent of budget use. This is, in turn, supported by the notion that the degree of participation derives from the perception of budgeting (Pasewark and Welker, 1990; Libby, 1999). Experienced entrepreneurs and managers perceive budgeting as an essential tool that aids their SMEs' performance. However, the minimal involvement of lower-level employees poses a threat to effective communication needed to drive budgets. Most respondents (75.9%) also admit that they use budgetary control systems tailored to their business needs.

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**Table 8 about here**

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Table 8 further indicates that most participants (78.3%) are satisfied with their businesses' budgetary control systems, suggesting that these SMEs establish appropriate budgetary controls. Similar to the findings in Table 4, SMEs use different budgetary controls depending on their business needs. A considerable number of respondents (74.2%) agree or strongly agree that budgetary controls are useful in allocating scarce resources and measuring business performance. This outcome ties with the impact of budgetary control on profitability as 74.1% of participants concur that effective budgetary control drives their profitability. Responses from Table 8 supports the broad use of budget control tools, with 68.3% stating that they utilise daily cash flow and expenditure reports to monitor day-to-day operations.

Table 9 presents some descriptive statistics for participants' perceptions of budgetary controls. Table 9 shows that the mean for all the elements is higher than 3.70, while the corresponding mode is 4 (frequently). The highest standard deviation score is  $\sigma = 1.023$  for budgetary controls as an essential tool in the effective management of SMEs, which is a statistically small standard deviation value. All other standard deviation elements scores are less than  $\sigma < 1.00$ , implying that they represent the mean and mode in the participants' response distribution. The outstanding results with the mean above 4.00 reflect the importance and impact of budgetary control systems on SMEs' business performance relative to profit generation. Furthermore, the results confirm the significance of maintaining formal financial records to gain satisfactory outcomes from budgetary control systems. Overall, the results imply that SMEs in the manufacturing sector have positive perceptions of budgetary control systems.

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**Table 9 about here**

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**Level of Education**

Budgetary controls reflect managers' educational status (O'Neil and Duker, 1986). Table 10 show that a sizeable number of respondents (31.8%) possess a bachelor's degree followed by

participants with a diploma qualification (30.0%), matriculation certificate (12.9%), masters' degree (14.1%) and a PhD (6.5%). The minority participants with no formal education constituted 1.2%, and those with a High School (Secondary) education constituted 2.6%. There are 0.6% of the participants with primary education as their highest level of education. In summary, more than 80.0% of participants are educated, evidenced by higher education qualification. The high level of qualification contradicts findings in O'Neil and Duker (1986), as the lack of education does not apply to this sample of manufacturing SMEs in South Africa with respect to budgeting. Findings from the preceding sections mirror SMEs' positive perception of budgetary controls systems, suggesting that the high literacy level encourages a positive budgeting and budgetary control perception. But these qualifications do not automatically translate to managerial competence, as SMEs may still lack the competence that prohibits them from effectively deploying formal control systems (Bianchi, 2002).

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#### **Table 10 about here**

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Table 10 shows that 128 participants from the sample agree/strongly agree that skilled and experienced managers implement budgetary controls. Observation from these findings relating to participants' level of education indicates that most participants possess the requisite education (university/college qualifications). Table 10 further confirms that 137 participants have higher education and training qualifications ranging from Diploma to PhD. Given the number of participants with a higher education qualification in the study sample (over 80%), we opine that the implementation of budgetary control is strongly associated with the possession of higher educational qualifications.

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#### **Table 11 about here**

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To further justify the above position, we cross-tabulate educational levels and budgetary controls implemented by skilled and experienced managers (see Table 11). Table 11 reveals no statistically significant difference between how participants perceive budgetary control among manufacturing SMEs. The majority of the participants across various education levels opine that budgeting and control require skill and experience. This could be due to their exposure to

budgeting and budgetary control processes in their organisations. Chi-square Tests (see Table 12) also shows a p-value above 0.05, which asserts no statistically significant difference (to support crosstabulation) between the perception of skilled and experienced managers implementing budgetary controls and level of education. This finding reinforces the notion that education and experience are positively related to the adoption and extent of deploying budgeting and budgetary control in organisations (Zor *et al.*, 2019).

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**Table 12 about here**

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### **Discussion of Findings and Study Implications**

Primarily, this study interrogates the influence of budgetary controls on manufacturing SMEs, relying on the South African context. Findings from this research shed useful insights into the divergent positions in the literature. Most literature on SMEs in developing economies (Aren and Sibindi, 2014; Rungani and Potgieter, 2018; Nwanyanwu and Ogbonnaya, 2018) suggests that the weak institutional environments in these economies contribute to poor performance among SMEs. While managerial ineptitude (Dumbu and Chadamoyo, 2012) and lack of financial support (Fatoki, 2014) have featured prominently in this conversation, this research's findings extend the debate. The results demonstrate that SMEs can preserve scarce financial resources by implementing robust budgetary controls. The implementation of budgetary controls profits from the relatively high literacy and managerial competencies of SME operators. In this instance, the study's findings are consistent with Enow and Kamala (2016), which reports that most South Africa SMEs manage their liquidity effectively. Ultimately, the results imply that budgetary control implementation is a critical indicator of South African SMEs' operational state.

Given these conclusions, it is apparent that clear organisational targets enhance business performance. The communication potential of budgets ensures that SMEs identify with corporate objectives and incentivised to attain these objectives. This outcome, which is reflected in the various responses summarised in Tables 6 to 9, corresponds with the central theme of GST, i.e., motivating the workforce to achieve corporate targets (Consolvo *et al.*, 2009). Furthermore, budgetary controls' communication power feeds into another core feature of GST, i.e., performance feedback (Locke and Latham, 2013), allowing organisations to

update (or revise) their targets as necessary while contributing to higher task performance. GST also combines goals, commitment and performance in ways that reflect a mutually beneficial relationship, indicating that agents' commitment to corporate goals maximises firm performance. Our data supports this position. We establish that when agents participate in establishing and implementing budgets, they are motivated to pursue and realise budget expectations while consistently evaluating themselves for opportunities to improve.

Drawing from our research, another concern that has trailed budgeting practices, particularly among SMEs, is the perception of its usefulness. Given SMEs' limited resources, SME operators tend to pay minimal attention to budgetary controls' impact on their operations (Enow and Kamala, 2016; Rungani and Potgieter, 2018). Such attitudes not only deny SMEs the opportunity to establish a robust management accounting architecture (budgetary control) but equally prevents SME decision-makers from taking advantage of the benefits that GST affords, i.e., goal setting. Contrastingly, our results suggest otherwise, as Tables 8 and 9 uncover widespread belief among SME operators in the capacity of budgetary controls to help achieve corporate goals. This outcome links with Enow and Kamala (2016) as such views maximise budgetary control's potential to drive positive business and improved performance. Furthermore, in agreement with Libby (1999), the extent of participation is significantly due to the perception of budgeting. More than 77% of participants affirm that SMEs' profitability rests on effective budgetary control systems, with another 70% suggesting that using a budgetary control model such as economic order quantity (EOQ) saves business costs.

While this study's findings reveal a positive perception of budgetary controls relative to SMEs' performance, GST embraces features prevalent in developed economies. This includes setting SMART objectives (Marsden and Richardson, 1994) and the nexus between setting goals and motivation (Ambrose and Kulik, 1999). The GST literature is yet to sufficiently incorporate variables in weak institutional contexts that may upset the expectations in Marsden and Richardson (1994) or Ambrose and Kulik (1999), for example. However, given the institutional challenges in the South African business environment, these problems have not contradicted the central themes of GST. While this may suggest that GST is context irrelevant, further research in this area would promote an understanding of the usefulness of GST as a theoretical anchor for studies investigating emerging phenomena (e.g., budgeting) in developing economies.



## **Summary and Conclusion**

This article investigated the influence of budgetary controls on SMEs' operations in the South African manufacturing sector. Data was collected via questionnaires and analysed through statistical means to address the research objectives. Our findings suggest that SMEs in the manufacturing industry vastly utilise budgetary control systems. Primarily, budgetary control systems are used for planning and monitoring organisational operations in pursuit of corporate goals. This study also finds that the extensive deployment of budgetary controls emerges from SME operators' perception of budgeting. These operators perceive budgeting as a cost control mechanism that permits planning and performance evaluation, thereby promoting the firm's wealth maximisation goals. Besides, the data also indicate that most SMEs review their budgets monthly. Given the dynamic South African business environment, operators are aware of the need to monitor consistently market development using budgets and budgetary controls to provide appropriate response mechanism. The preceding activity means that when budgets deviate from plans, SMEs can uncover the source of the deviation and subsequently implement revised budgetary controls that minimise future budget deviations.

However, the data hints that SMEs seldom use manufacturing budgets even though study respondents were operators from SMEs in the manufacturing sector. Also, a significant number of SMEs seek external assistance in rectifying budget deviations by outsourcing the budgeting function. While the challenges in outsourcing are well documented (see Nordin, 2006), seeking external help in fixing budget deviations may increase costs in the long run. Outsourcing could also impact firm competitiveness as core business information may be divulged.

While this study achieved its objectives, it is essential to note the study's limitation. This research's primary limitation is the non-inclusion of the income statement and balance sheet in the analysis. While SMEs engage with these two financial statements, we observe that the literature has consistently ignored other corporate performance variables, hence the focus on these less-researched budgeting variables. Given the reported findings, we believe that this study offers insights that extend existing discourse in this research field.

Based on our findings, we articulate two recommendations for SMEs. First, we advocate increased managerial training for SME operators in the area of budgeting. A substantial element of the training should provide SME operators with the competence to address budget deviations internally, in a cost-efficient manner. This enhances their knowledge and perception of budgetary controls in the long term and ensures flexibility and timeliness in responding to

changes in the business environment. Second, the data highlights the low engagement of employees in budgetary control processes. Non-participation in budgeting impedes a critical function of budgeting, i.e., a medium of communication. This issue also has adverse effect on the perception of budgeting. Therefore, we propose a blend of the top-down and bottom-up budgeting process that ensures a continuous exchange of budgeting information and facilitates an organisation-wide awareness of budgetary controls within an organisation. Such procedures must ensure greater participation in the budgeting process by all levels of employees.

The above recommendations, the nexus between GST and budgeting, and the insights from this study provide opportunities to contribute to this research domain. Bearing in mind that this research focused on behavioural (impact and perception) elements of budgetary controls, researchers are encouraged to employ an alternative methodology to investigate the impact of budgetary controls on SMEs' performance. Such studies could explore how budgetary controls (using relevant variables, some of which have been identified in this research) affect key performance variables (e.g., return on assets) among SMEs. Also, given that this study adopts the South African context, an alternative stream of research may undertake a broader investigation, relying on data from varieties of capitalism, to understand how institutional variations in business environments mediate the relationship between budgetary controls and SMEs performance. The authors are also cautious about generalising the result of this study. A national survey or studies from various provinces may help provide a clear picture of the SMEs level of education and whether the outcomes in Cape Town is consistent with similar contexts across the globe. Lastly, this research highlighted the marginal interest paid to the manufacturing budget by manufacturing SMEs. We invite scholars to note this indifference by employing appropriate techniques to generate insights that clarify this apathy.

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